STATE OF IOWA

DEPARTMENT OF COMMERCE

UTILITIES BOARD

IN RE: MIDAMERICAN ENERGY COMPANY	DOCKET NO. RPU-02-2

ORDER SCHEDULING HEARING ON MATERIAL ISSUES OF FACT CONCERNING SETTLEMENT

(Issued August 30, 2002)

PROCEDURAL BACKGROUND

On March 15, 2002, MidAmerican Energy Company (MidAmerican) filed with the Utilities Board (Board) proposed gas tariffs, identified as TF-02-115 and TF-02-116. In TF-02-115, MidAmerican proposed a temporary increase that would produce additional revenue of approximately $20.4 million. In TF-02-116, MidAmerican proposed a permanent annual revenue increase of approximately $26.6 million, or an overall annual revenue increase of 4.3 percent. The Board docketed the proposed temporary and permanent rate increases as Docket No. RPU-02-2.

The Board, on June 12, 2002, issued an order approving a temporary rate increase of $13,823,286, not to exceed $696,981,107. The temporary rate increase was calculated based upon an overall rate of return of 9.394 percent and a return on common equity of 11.3 percent.

On July 15, 2002, all parties to this proceeding, except for Keith E. Meyer, filed a "Settlement Agreement" proposing to settle all outstanding issues with regard

to MidAmerican's permanent rate increase request. The settlement, if approved, would allow MidAmerican to increase natural gas rates by approximately $17,746,034.

On August 14, 2002, Mr. Meyer filed his protest of the settlement as required by 199 IAC 7.2(11)"c." The Board issued an order shortening time for reply comments, and on August 16, 2002, MidAmerican and the Consumer Advocate Division of the Department of Justice (Consumer Advocate) filed reply comments. MidAmerican and Consumer Advocate support the "Settlement Agreement" and contend that the settlement meets all of the requirements of 199 IAC 7.2(11) and none of the issues raised by Mr. Meyer rise to the level of being an issue of material fact for which a hearing is required.

The issues raised by Mr. Meyer in his comments contesting the settlement will be addressed below.

CONTESTED ISSUES

1. Mr. Meyer contends that the settlement process was not conducive to participation in a professional manner. MidAmerican contends that Mr. Meyer had a full opportunity to participate in the negotiations concerning the permanent rate increase. All parties were included in the negotiations from the beginning of the process which is a significant difference from past rate cases. MidAmerican then objects to the references made by Mr. Meyer concerning the negotiations and states that a party does not have to join the settlement.

Consumer Advocate suggests it is limited in its ability to comment on Mr. Meyer's comments concerning the negotiations since those negotiations are confidential and privileged communications under 199 IAC 7.2(11)"g."

2. Mr. Meyer contends that the return on common equity in the settlement of 10.75 percent is excessive. He cites to a statement purportedly made by Warren Buffett, CEO of Berkshire Hathaway Inc. and the principal shareholder of MidAmerican's parent, MidAmerican Energy Holdings Company, that utilities projecting 11 percent returns on common equity were high. Mr. Meyer points out that Consumer Advocate in a proceeding involving another utility in July 2002 recommended a 9.65 percent return on common equity.

Mr. Meyer then contends that the analysis of MidAmerican witness Dr. James H. Vander Weide in his prefiled testimony is flawed. Mr. Meyer suggests that Dr. Vander Weide did not use a correct set of comparative companies in his Discount Cash Flow (DCF) analysis and Dr. Vander Weide's analysis of risk premiums did not address non-linear changes or structural breaks.

MidAmerican suggests that the comments of Warren Buffett and filings in other cases by Consumer Advocate referenced by Mr. Meyer are not relevant to this proceeding. MidAmerican compares the 10.75 percent return on common equity in the settlement with the 11.3 percent return approved by the Board for temporary rates.

MidAmerican then discusses Mr. Meyer's criticisms of Dr. Vander Weide's DCF analysis and linear study of risk premiums. MidAmerican suggests that

Mr. Meyer did not understand Dr. Vander Weide's testimony and Dr. Vander Weide properly applied his analysis to companies comparable in risk to MidAmerican. MidAmerican goes into some detail concerning the validity of Dr. Vander Weide's analysis. MidAmerican contends that no non-linear or structural break relationship exists in the data. Finally, MidAmerican points out that Dr. Vander Weide's testimony supports a return on equity of 12.6 percent which is not contained in the settlement and the 10.75 percent proposed in the settlement is below MidAmerican's initial request and the interim return on equity approved by the Board.

Consumer Advocate makes the same two points as MidAmerican described in the above paragraph and points out that the Board found a range of 10.07 to 12.07 percent was reasonable in establishing temporary rates and the 10.75 percent is within that range.

3. Mr. Meyer alleges that MidAmerican has a history of ignoring Board rulings. He cites a Board decision in MidAmerican Energy Company, Docket Nos. RPU-01-3 and RPU-01-5, “Order Approving Settlement with Modifications,” p. 10 (Dec. 21, 2001), in which the Board held that reference to a "rate freeze" was not appropriate. Mr. Meyer then points out that MidAmerican referred to a "rate freeze" in a subsequent filing with the Securities and Exchange Commission (SEC).

MidAmerican contends that it has properly referred to its electric rate increase. MidAmerican explains that it used the term "rate freeze" in the SEC filing as a shorthand description of the effect of the settlement in that case on revenues.

Consumer Advocate suggests that although the use of the term "rate freeze" may have been unfortunate, MidAmerican's use of the term does not appear to be in disregard of the Board's order.

4. Mr. Meyer suggests that the settlement is not consistent with past Board rulings on price disparities within a company. He contends that the Board has held that price disparities due to historical or geographical circumstances rather than cost of service need to be addressed.

MidAmerican asserts that the settlement properly balances the elimination of price disparities and rate shock to customers. MidAmerican points out that the process of designing rates to mitigate rate shock and move toward elimination of price disparities is included in the settlement. MidAmerican then provides examples of how the settlement balances the two goals.

Consumer Advocate acknowledges the Board precedent to minimize or eliminate inter-zonal rate disparities that are based on historical and geographical issues rather than cost of service. Consumer Advocate contends that the settlement makes progress toward equalization of rates between MidAmerican's east and west zones.

6. Mr. Meyer proposes that the length of time before MidAmerican can file another rate increase should be longer than two years. He suggests that MidAmerican's rates be adjusted for inflation in the third, fourth, and fifth year after the rate increase in this proceeding are set.

MidAmerican states that the two-year rate freeze was a negotiated part of the settlement entered into voluntarily by MidAmerican. MidAmerican points out that Mr. Meyer's proposal could provide higher rates than MidAmerican would otherwise be allowed by the Board.

Consumer Advocate agrees with MidAmerican that the two-year rate freeze is voluntary and MidAmerican did not have to agree to this provision of the settlement.

7. Mr. Meyer then proposes that the Board hold evidentiary hearings to examine all aspects of the rate increase request, including testimony by MidAmerican's owner and auditors. The reference to the owner, Warren Buffett, and the auditors, Deloitte & Touche, LLP, relates to his motions to have these persons appear and testify at the hearing. These motions will be addressed below.

MidAmerican suggests that the issues of new ownership were reviewed by the Board in Docket Nos. SPU-98-8 and SPU-99-32 and these issues do not need to be relitigated in this docket. MidAmerican states that rates are based upon the cost of service in this docket and not on the costs of MidAmerican's parent corporation.

Consumer Advocate states that although a full litigation of all aspects of the permanent rate request would provide a fuller record, this does not rebut the position of the signatory parties that the settlement satisfies the requirements of 199 IAC 7.2(11).

BOARD DISCUSSION OF ISSUES

Settlement agreements in contested cases involving requests for permanent rate increases by rate-regulated public utilities are governed by the provisions of Board rules found in 199 IAC 7.2(11). These rules provide that the Board will not approve settlements, whether contested or uncontested, unless the settlement is reasonable in light of the whole record, consistent with law, and in the public interest. Paragraph 7.2(11)"d" states that a party who is not a signatory to a proposed settlement must file comments concerning the portions of the settlement that the party opposes, the legal basis for the opposition, and the factual issues that it contests.

Paragraph 7.2(11)"e" provides if a proposed settlement is contested, in whole or in part, on any material issue of fact, the Board may schedule a hearing on the contested issues. This paragraph also provides that the Board may decline to schedule a hearing where the contested issue of fact is not material or where if the contested issue is one of law.

Finally, paragraph 7.2(11)"g" provides that any discussion, admission, concession, or offer to settle oral or in writing made during any negotiation or settlement are privileged and inadmissible in a proceeding before the Board.

The seven issues contested by Mr. Meyer described above must be weighed based upon these standards.

1. The Board finds that the provisions of 199 IAC 7.2(11)"g" prevent the Board from considering the issue of the conduct of the parties or any discussions of

the parties during settlement negotiations. Even though Mr. Meyer's comments may not relate to a substantive issue of the settlement, they are discussions of the settlement process and as such should not be revealed and are inadmissible to contest the settlement.

2. The Board finds that Mr. Meyer raises a material issue of fact with his challenge to the return on common equity agreed to by the parties. Mr. Meyer claims the analysis of MidAmerican witness Dr. Vander Weide supporting MidAmerican's requested return on equity is flawed. Even though the return on common equity of 10.75 percent in the settlement is well below that supported by Dr. Vander Weide in his testimony, the appropriate return on common equity is a material issue of fact in this proceeding. In reaching a decision on the settlement, the Board will be required to determine whether the settlement based upon a 10.75 percent return on common equity is reasonable. Mr. Meyer should be given the opportunity to cross-examine Dr. Vander Weide on his analysis and the 10.75 percent return in the settlement.

3. The Board finds that the issue concerning whether MidAmerican did not properly follow the Board's decision in MidAmerican Energy Company, Docket Nos. RPU-01-3 and RPU-01-5, is not a material issue of fact relating to whether the Board should approve the settlement. Even if the Board were to find that MidAmerican improperly used the term "rate freeze" in the SEC filing, it would have no bearing on the reasonableness of the rates proposed in the settlement.

4. The Board finds that Mr. Meyer raises a material fact issue with regard to rate disparities between zones even though he does not point to any specific rates

that he believes should have been increased or decreased to accomplish uniformity. MidAmerican and Consumer Advocate agree that the Board has indicated in past orders that eliminating rate disparities based upon history or geography is in the public interest. MidAmerican and Consumer Advocate also agree that this policy should be balanced with possible rate shock to customers.

The settlement provides some movement to eliminate rate disparities between MidAmerican's east and west zones. For residential and general service customers, east-west energy rate differentials for the first 250 therms of monthly use will be reduced from 7.5 cents to 3.7 cents. For additional usage above 250 therms, the rate differentials will generally be eliminated. For large volume transport customers (west rate LT and east rate 90) average rate differentials will be reduced by 40 percent, while limiting LT rate increases to 20 percent. Also, west zone customers will be offered a new large volume demand rate and a new seasonal rate, identical to those in the east zone. Mr. Meyer will be provided the opportunity to cross-examine MidAmerican witness Gregory C. Shaefer concerning the existing rate disparities and the movement toward elimination of these disparities proposed in the settlement.

5. The Board finds that Mr. Meyer's contention that the period of time before MidAmerican can file for another rate increase should be more than two years is not a material fact issue. MidAmerican is under no legal obligation to refrain from filing a general rate case for two years and agreed to the moratorium voluntarily as part of the settlement. If the case were to be litigated, the Board could not order

MidAmerican to refrain from filing another rate case for two years. Iowa Code § 476.6(10) contains the only limitations on filing another general rate increase application.

6. The Board finds MidAmerican's two changes in ownership since the last rate case does not present a material issue of fact requiring litigation of every aspect of the settlement as proposed by Mr. Meyer. The issues concerning the two changes in ownership were reviewed in Docket Nos. SPU-98-8 and SPU-99-32. Mr. Meyer has failed to raise a material fact issue that would require the Board to hold an evidentiary hearing concerning the changes in ownership.

REQUEST FOR APPEARANCE OF PRINCIPAL OWNER

Mr. Meyer has requested that the Board order Warren Buffett to appear and testify to reconcile conflicting public positions as to expected rate of return. MidAmerican objects to the request stating that 1) Mr. Buffett is not the prinicipal owner of MidAmerican but the principal owner of Berkshire Hathaway Inc., the largest stockholder of MidAmerican Holdings Company, the parent of MidAmerican, 2) it has two expert witnesses on rate of return and Mr. Buffett's comments are irrelevant to the return on common equity for MidAmerican, and 3) that there is no precedent for requiring the appearance of a stockholder and it would be bad public policy to require Mr. Buffett to appear.

The Board finds that Mr. Buffett's testimony concerning the basis for his statements concerning rate of return might be interesting but would be of minimal

substantive value on this issue. MidAmerican has presented the testimony of two experts on the issue of rate of return and capital structure and did not offer Mr. Buffett as a witness. Without a compelling reason to require the testimony of a shareholder, regardless of the number of shares he controls, the Board should not force MidAmerican to produce a shareholder witness the company has not sponsored.

REQUEST FOR APPEARANCE OF ACCOUNTANTS

Mr. Meyer has requested the appearance of the accounting firm Deloitte & Touche, LLP, at a hearing to respond to questions concerning the standards by which the audit of MidAmerican was conducted and to explain the relationship between Deloitte & Touche, LLP, and MidAmerican. MidAmerican opposes this request. First, MidAmerican argues that the request is untimely since it was filed July 22, 2002, and Mr. Meyer was required to prefile his testimony on June 24, 2002. Second, MidAmerican contends that there is no suggestion in the record for a need to call the accounting firm. No other intervenors have expressed a concern with the audit performed by Deloitte & Touche, LLP, and there was no issue raised in the settlement regarding the audit.

The Board finds that there is no suggestion raised by any party, other than Mr. Meyer, that the audit performed by Deloitte & Touche, LLP, was not properly conducted. If Mr. Meyer had a concern about the audit he should have raised it in his prefiled testimony.

PROCEDURE FOR HEARING

The Board will schedule a hearing to address the two issues found by the Board to be issues of material fact. MidAmerican shall produce Dr. James H. Vander Weide for cross-examination on the issue of return on common equity and Gregory C. Shaefer on the issue of rate disparities. Mr. Meyer may produce a witness on each of these issues. MidAmerican and Mr. Meyer may offer direct testimony of these witnesses or may just offer the witnesses for cross-examination. MidAmerican witnesses will testify first and be subject to cross-examination by Mr. Meyer and the other parties. Then Mr. Meyer's witness will testify and be subject to cross-examination. Testimony on other issues or cross-examination on other issues will not be allowed. The previously ordered procedural schedule is superseded by these procedures.

Mr. Meyers will be required to file the names and credentials of his witnesses.

ORDERING CLAUSE

IT IS THEREFORE ORDERED:

1. A hearing shall be held beginning at 10 a.m. on September 16, 2002, for the purpose of receiving testimony and cross-examination of witnesses on the contested issues of return on common equity and rate disparities as discussed in the body of this order. The hearing shall be held in the Utilities Board Hearing Room, 350 Maple Street, Des Moines, Iowa. The parties shall appear one-half hour prior to the time of the hearing for the purpose of marking exhibits. Persons with disabilities

requiring assistive services or devices to observe or participate should contact the Utilities Board at (515) 281-5256 in advance of the scheduled date to request that appropriate arrangements be made.

2. On or before September 6, 2002, Mr. Meyers shall file the names and credentials of any witnesses he intends to offer.

UTILITIES BOARD

/s/ Diane Munns

/s/ Mark O. Lambert

ATTEST:

/s/ Sharon Mayer
Executive Secretary, Assistant to

/s/ Elliott Smith

Dated at Des Moines, Iowa, this 30th day of August, 2002.